

No. 17,352

IN THE

United States Court of Appeals  
For the Ninth Circuit

FARMERS UNION CORPORATION,

*Petitioner,*

VS.

COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

On Petition for Review of the Decision of the  
Tax Court of the United States

REPLY BRIEF FOR PETITIONER

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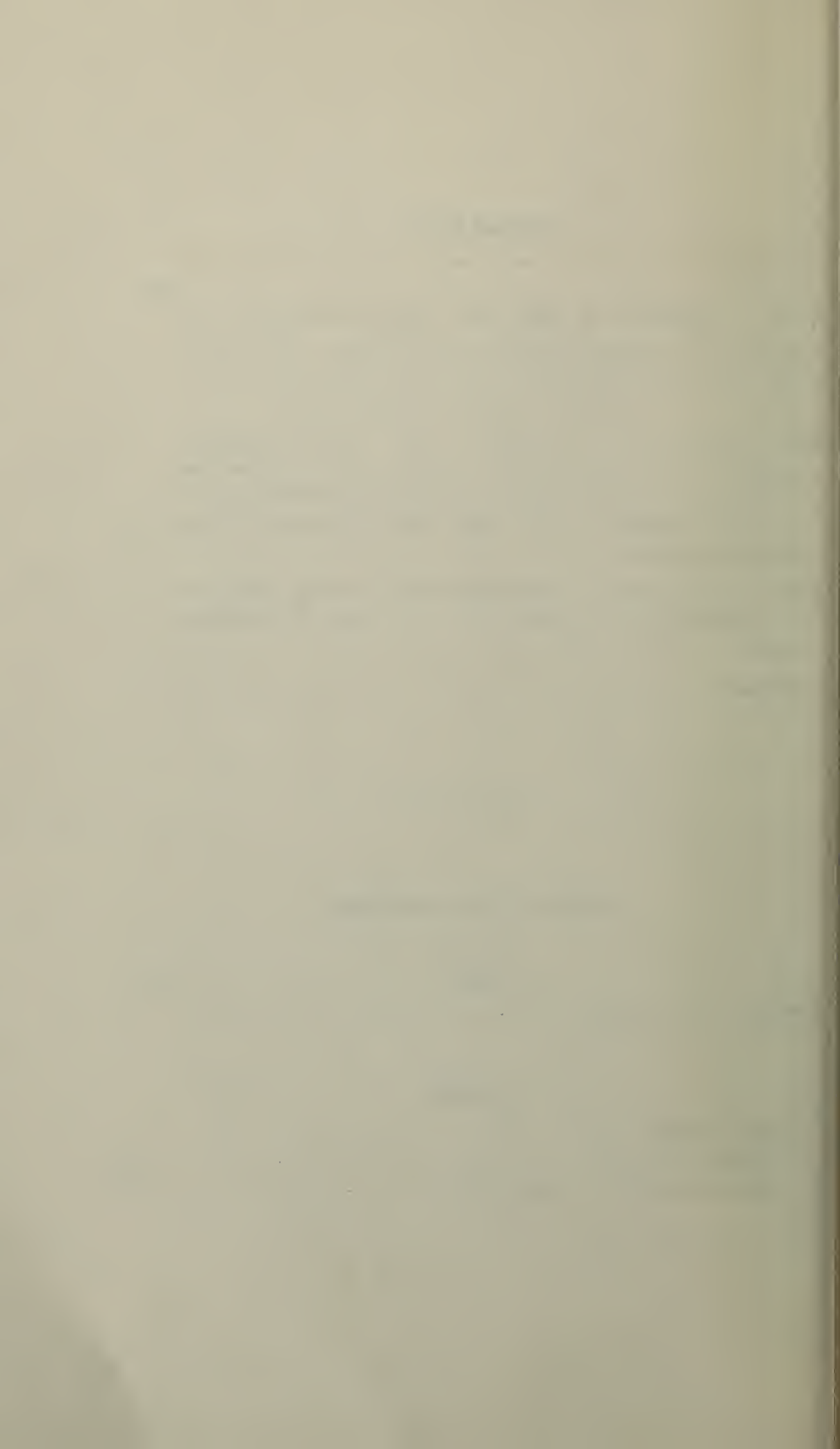
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**REPLY BRIEF FOR PETITIONER**

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REPLY TO ARGUMENT OF RESPONDENT THAT THE DISTRIBUTION OF TAXPAYER'S MERCANTILE BUSINESS IN EXCHANGE FOR CAPITAL STOCK WAS A PARTIAL LIQUIDATION RATHER THAN A SALE, AND, THEREFORE, NO GAIN OR LOSS WAS REALIZED THEREBY.

The brief for respondent, generally paraphrases the decision of the Tax Court on this point, with additional emphasis upon one of the minutes of petitioner that used the word "liquidation" and reliance upon the doctrine of "business contraction" as evidence of the exchange in question being a partial liquidation.

In extension of the argument of petitioner in its opening brief, it may be noted (1) that other minutes of the petitioner contained the words "sale" and

“segregation by sale”; (2) that notification to the stockholders of the plan adopted by the board of directors was accompanied by an “offer” to exchange corporation property for stock; and (3) that financial statement, issued concurrently, contained a list describing and evaluating the items “to be sold”. These facts, when added to the substantial evidence of intent of the petitioner to sell some of its assets, rather than to engage in a “mere distribution of its assets in kind in partial or complete liquidation . . .” (Section 22(a)-20, I. R. C., 1939) would tend to reduce the significance of respondent’s contention in this regard.

Respondent cites no authority to support his conclusion that contraction of business, as a result of any transaction, would require that such transaction be identified as a partial liquidation, under the 1939 Internal Revenue Code.

Respondent argues that reduction of stated capital and cancellation or retirement of the stock acquired by petitioner are additional reasons for concluding that the subject transaction was a distribution in liquidation. There is no evidence that the stock, so acquired, was cancelled or retired or that it was negotiated and obtained for that purpose. Accordingly, the capital structure of the petitioner remained the same. (See statutes and cases cited in petitioner’s opening brief.)

The preponderance of the evidence in the record firmly establishes this transaction as a negotiated sale of specified corporation property in which the stock involved was received as consideration therefor.

REPLY TO ARGUMENT OF RESPONDENT THAT EVEN IF TAX-PAYER'S DISTRIBUTION OF THE MERCANTILE BUSINESS WERE A SALE, NO LOSS IS ALLOWABLE ON THIS TRANSACTION BECAUSE THE DISTRIBUTEES OF TAXPAYER'S PROPERTY OWNED MORE THAN 50 PERCENT OF ITS OUTSTANDING STOCK.

On September 17, 1958, approximately three weeks before trial, respondent served an amendment to answer in which it was alleged that if the sale alleged in the petition did, in fact, occur, petitioner would still not be entitled to a loss deduction because of the provisions of Section 24(b) and 24(b)(2)(c) of the Internal Revenue Code of 1939 (R. 9-10).

At the outset of the trial, during the opening statement for petitioner, the alternative or conflicting issues were called to the attention of the Court. After some colloquy, the Court agreed that respondent would be required to elect to prove either that the transaction was a distribution in liquidation and not a sale or concede that there was a sale but to a related interest, under 24(b), I. R. C. (1939) (R. 19-21).

At no time, during the trial, was the question of possible sale to a related interest at issue. No documentary evidence was introduced in proffered proof of such a sale and the only testimony, that had any bearing on the subject, was given by Mr. McEnery (R. 84-88) and Mr. Benson (R. 157-158) who, on direct examination, described their separate and unrelated actions in acquiring their respective interests in the property offered by the corporation.

No mention was made of the subject in the decision of the Tax Court, except to state that the conclusion

reached made it “unnecessary to consider other arguments and related questions which have been presented by both parties” (R. 293). Accordingly, it is respectfully submitted that there is no issue or decision of the Tax Court involving the application of the aforesaid Section 24(b), that can properly be made the subject of review by or appeal to this Circuit Court of Appeals. *Rhodes*, 111 F. 2d 53.

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REPLY TO ARGUMENT OF RESPONDENT THAT TAXPAYER  
FAILED TO DEMONSTRATE THAT IT SUFFERED ANY  
ACTUAL LOSS ON THE TRANSACTION.

Respondent bases this argument on the well established principle that gain or loss, in a taxable exchange, is measured by the difference between the adjusted cost of the property transferred and the market value of the property received. The validity of the adjusted cost of the property transferred has not been questioned—only the market value of the stock received in the subject transaction is alleged to be undetermined.

The record discloses that petitioner made a written offer (Exhibit 2-B) of clearly described property for shares of stock to be evaluated at Ten Dollars per share (par value). This offer was made to every stockholder.

Under an ancient rule, market value is the price that a willing buyer and a willing seller agree upon when neither of them is under any compulsion to act. Petitioner's stock was not listed on any exchange and

there were no recent transactions (other than those mentioned by Mr. McEnery) from which to obtain pertinent data.

Consequently, petitioner used the only method available to determine whether there were 8,000 shares of stock outstanding that had an agreed value of Ten Dollars per share.

The record also discloses that the property offered by petitioner had a lower market value than its adjusted cost. This fact was known to the stockholders at the time the offer was made. Therefore, from the standpoint of both petitioner and stockholder, all of the elements of the accurate establishment of market value were present.

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#### CONCLUSION

It is respectfully submitted that the Tax Court was in error in the specifications heretofore set forth and judgment should be rendered in favor of petitioner.

Dated, San Mateo, California,  
November 6, 1961.

Respectfully submitted,  
RALPH A. YEO,  
*Attorney for Petitioner.*

